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**OFFICE OF INSPECTOR GENERAL**  
for the Millennium Challenge Corporation

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**AUDIT OF THE MILLENNIUM  
CHALLENGE CORPORATION'S  
MANAGEMENT OF ITS  
CONDITIONS PRECEDENT IN  
ITS COMPACT AGREEMENTS**

AUDIT REPORT NO. M-000-07-002-P  
July 26, 2007

WASHINGTON, DC



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FROM THE AMERICAN PEOPLE

*Office of Inspector General  
for the  
Millennium Challenge Corporation*

July 26, 2007

The Honorable John J. Danilovich  
Chief Executive Officer  
Millennium Challenge Corporation  
875 Fifteenth Street, NW  
Washington, DC 20005

Dear Ambassador Danilovich:

This letter transmits the Office of the Inspector General's final report on the Audit of the Millennium Challenge Corporation's Management of Its Conditions Precedent in Its Compact Agreements. In finalizing the report, we considered your written comments on our draft report and included those comments in their entirety in Appendix II of this report.

The report contains three audit recommendations for corrective action. Based on your response to our draft report, we consider that a management decision has been reached on the recommendations. Final action for the recommendations must be determined by the MCC, and we ask that we be notified of the MCC's actions.

I appreciate the cooperation and courtesy extended to my staff during this audit.

Sincerely,

John M. Phee /s/  
Assistant Inspector General  
Millennium Challenge Corporation

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# SUMMARY OF RESULTS

The Assistant Inspector General for the Millennium Challenge Corporation (MCC) conducted the Audit of the Millennium Challenge Corporation's Management of Its Conditions Precedent in Its Compact Agreements as part of its fiscal year 2007 audit plan. The audit was conducted to determine whether MCC ensured that all required conditions precedent (CPs) were met before compacts went into effect or disbursements were made to compact countries (see page 3).

MCC requires that the compact country meet a series of CPs before a compact is entered into force<sup>1</sup> and before initial and subsequent funds are disbursed for compact implementation. These CPs are established in conjunction with the compact country by MCC's legal and sector experts during compact negotiations and are outlined in the compact and related disbursement agreements. The purpose of a CP is to ensure that (1) the compact countries establish certain legal, budgetary, and program actions and (2) the various programs being funded by MCC are implemented and carried out with proper controls.

The audit found that MCC ensured that all CPs were successfully met and properly implemented before the compact was entered into force and before the funding of initial and subsequent disbursements (see page 4). However, the audit identified three areas in which MCC could improve its CP process. Specifically, MCC needs to develop a more formalized and consistent approach to guide compact countries in revising and reporting on CPs (see page 4). Additionally, MCC's clearance timeframes for approval of country requests, which include the CP report, could be clarified (see page 6). The audit also identified the need for additional documentation to justify a procurement action (see page 7).

In its response to our draft report, the MCC agreed with the recommendations and explained its plan for implementing the recommendations. Therefore, we consider that a management decision had been reached on the recommendations (See page 10).

Management comments are included in their entirety in appendix II (see page 13).

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<sup>1</sup> According to MCC officials, entry into force is the point at which a binding commitment is recognized and the compact funds are obligated.

# BACKGROUND

The Millennium Challenge Corporation (MCC) was established in January 2004 by the Millennium Challenge Act of 2003 to provide assistance to eligible developing countries that rule justly, invest in their people, and encourage economic freedom. This assistance is provided through compact agreements<sup>2</sup> between MCC acting as a U.S Government agency and recipient country governments. As of April 2007, MCC had signed compacts with 11 countries for approximately \$2.9 billion.

After an eligible country and MCC formally sign a compact, the country must meet a series of conditions precedent (CPs)<sup>3</sup> established by MCC before the compact can enter into force and before initial and subsequent funds can be disbursed for the compact implementation and other related activities. The purpose of these CPs is to ensure that (1) the eligible country's compact and compact activities have met established MCC requirements for implementation and (2) the compact activities will be implemented properly. MCC is not obligated to disburse funding for compact activities if an eligible country does not meet its CP requirements to MCC's satisfaction.

CPs are primarily established in conjunction with the compact country by MCC's legal and sector experts during compact negotiations and are generally country and project specific. Certain CPs must be met before the compact is entered into force, and a set of conditions must be met before initial and subsequent disbursements. CPs established for entry into force require the country to meet several criteria, including the following: (1) establish an accountable entity, (2) develop systems for financial control and oversight, (3) finalize postcompact legal documents, and (4) develop an approved disbursement agreement. CPs related to initial and subsequent disbursements must satisfy, or ensure the satisfaction of, all applicable CPs in the countries' disbursement agreement. Examples of these CPs include establishing a bank account, developing an interim procurement plan approved by MCC, and developing an approved fiscal accountability plan.

CPs are documented in the compact country's compact and disbursement agreements. CPs within the disbursement agreements may be modified annually by MCC and the compact country.

MCC reserves the right to waive or defer CPs. For MCC to do this, the compact country must make a formal request to MCC and include the reasons for the request and the material impact, if any, the waiver may have on the compact activities.

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<sup>2</sup> A compact is a multiyear agreement between MCC and an eligible country to fund specific programs targeted at reducing poverty and stimulating economic growth.

<sup>3</sup> A conditions precedent is an act or event (other than a lapse of time) that, unless the condition is excused, must occur before a duty to perform a promise in the agreement arises.

## **AUDIT OBJECTIVE**

The Assistant Inspector General for MCC conducted this audit as part of its fiscal year 2007 annual audit plan. The objective of this audit was to answer the following question:

Did the Millennium Challenge Corporation ensure that all conditions precedent were successfully met and properly implemented before the compact was entered into force and initial disbursements and subsequent disbursements were made to the compact country?

Appendix I contains a discussion of the audit's scope and methodology.

# AUDIT FINDINGS

Overall, for the countries included in this review,<sup>4</sup> the audit found that MCC ensured that all CPs were successfully met and properly implemented before the compact entered into force and before initial and subsequent disbursements were made to the compact country.

Satisfactory completion of these actions is evidenced by MCC and the country executing a number of documents specified in the compact, such as a governance agreement, a fiscal agent agreement, and incumbency and specimen certificates from MCC and the compact country. For the countries included in our review, the required documents were completed and approved before the countries' compacts entered into force and before disbursements were made. In one country, a CP had not been completed or deferred. The CP should have been completed or deferred by the third quarter ending June 2006; however, the compact country had not requested that the CP be deferred because of an oversight in its tracking. As this was the only case involving a CP that did not receive an approval for a deferral when required, no recommendation is made.

The audit did identify areas within the CP process for which MCC could strengthen its overall policies, procedures, and guidance. These areas include the process used for revising and reporting of CPs and specifying clearance timeframes for approvals of country requests. The audit also identified areas within the procurement process that could be improved. One such area concerned the absence of adequate documentation for procurement actions. The problem areas are discussed below.

## **Process Used to Revise Conditions Precedent Should Be Formalized**

Summary: MCC did not have a consistent and documented process for a compact country to properly revise and report on its CPs, because MCC was reviewing the CP process and had not yet developed written guidance. The current process used to revise and report on the CPs was a result of MCC incorporating lessons learned from prior compact countries. According to internal controls established by the General Accountability Office (GAO), for an entity to run and control its operations, it must have relevant, reliable, and timely communications. The internal controls also state that pertinent information should be identified, captured, and distributed in a form and timeframe that permits people to perform their duties efficiently. Until MCC formally establishes and provides relevant and consistent guidelines to its staff and compact countries on revising and reporting on CPs, the compact activities could be delayed or not implemented as required.

Although MCC had a process to establish the CPs in its country compacts and related disbursement agreements, the audit identified various methods the compact countries used in revising and reporting on the CPs.

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<sup>4</sup> Armenia, Cape Verde, Georgia, Honduras, Madagascar, and Nicaragua.

First, initial CPs contained in the disbursement agreement were reflected on a CP schedule that described the CP, along with a specific quarterly and yearly timeframe for meeting the CP. Once a compact country started implementation of the compact activities, both MCC and the compact country felt a need to revise the CP schedule for various reasons, such as to adjust the timeframes for completion of the CPs. Compact countries are required to conduct an annual evaluation of the CPs and work with their counterpart in MCC to confirm the relevancy of the CP and the timeframes. During the required annual review of CPs, the staff in Honduras removed the timeframes for meeting CPs altogether and instead included a statement that, until the CP had been met, MCC would not fund the specific project or activity. The staff in Georgia retained its existing CP schedule format and worked with MCC sector counterparts to determine which CPs were required within a specific quarter during the second year of the compact. In Cape Verde, the staff revised its CPs for a particular project but had not obtained MCC's approval for the revisions and was unsure of the process to obtain approval.

Second, some countries were informally moving program-specific CPs to the country's program work plans. For example, MCC staff in Nicaragua stated that MCC wanted to reevaluate the CPs to ensure that they were still relevant and modify them as needed to ensure that they were the right controls for ensuring that the compact achieved its intended results. The staff also considered moving the less critical CPs into the work plans. Likewise, in Cape Verde, the staff was working to include the activity-level CPs in the work plan. Because of the high number of CPs, the staff was working to reduce and modify these conditions by collapsing certain CPs into one or by changing the CP's requirements. In Honduras, the staff moved some program-type CPs (such as developing a resettlement plan or moving telephone poles before road construction) from the initial CP reporting document to the country's work plan.

Third, countries differed in the way they requested deferrals for CPs that were required during a specific quarter. Unlike Georgia, Honduras, and Nicaragua, which submit a formal letter to request a CP deferral, Millennium Challenge Account–Cape Verde (MCA-Cape Verde) did not submit a formal letter to request deferrals and only submitted its request on the last column of its CP schedule. In the cases of Georgia, Honduras, and Nicaragua, the country request letter contained a statement that, if MCC concurred with the deferral request, then MCC was to sign the request letter and return it to the respective country. When asked about how they received approvals from MCC, officials at MCA-Cape Verde stated that they usually requested revised deferrals from their MCC counterpart via phone or e-mail, but no documentation was available to show MCC's approval of the deferrals.

According to MCC officials, no guidance documents were in place on revising and reporting CPs. An MCC official added that MCC's senior management was aware of this and had discussed the issue at a recent senior management offsite meeting. Currently, MCC transaction teams are learning from one another and looking at the efforts put into developing, revising, and reporting on CPs for newer countries to determine whether these approaches will work for other countries. Another MCC official stated that the goal of MCC is to unclutter the compact by categorizing CPs meant for the recipient country and those geared toward the specific projects as outlined in the compact.

According to GAO standards for internal controls, to run and control its operations, an entity must have relevant, reliable, and timely communications relating to internal as well



as external events. Information is needed throughout the agency to achieve all of its objectives. GAO also states that pertinent information should be identified, captured, and distributed in a form and timeframe that permits people to perform their duties efficiently.

CPs are internal controls set up to ensure the successful implementation of the compact activities. Unless MCC formally establishes and provides guidelines to its staff and personnel from compact countries on the procedures to revise and report on CPs, it is more likely that the CPs will not be met. In turn, the likelihood is greater that the compact activities will not be implemented successfully. Therefore, we are making the following recommendation:

***Recommendation 1:*** We recommend that the Deputy Chief Executive Officer, by means of the current Implementation Working Group or a newly established working group, develop and issue, specific guidelines that describe how conditions precedent will be established, defined, revised, and reported.

## **Clearance Timeframes Could Be Better Communicated**

Summary: MCC's timeframes for reviewing and approving compact country disbursement requests were not clear. MCC's instructions, which accompanied a June 2006 clearance matrix, indicated that MCC had 5 days to clear country requests. The instructions did not clearly identify which country requests the 5 days pertained to, however; as a result, there was confusion on the amount of time that MCC had to clear disbursement requests that included the CP schedule. According to MCC officials, the 5 days indicated in the instructions related only to procurement requests. MCC agreed that the 5-day requirement in the instructions did not clearly define which country request was being referenced. GAO's Internal Control Standards state that information should be recorded and communicated to management and others within the entity who need such information in a form and within a timeframe that enables them to carry out their internal control and other responsibilities. The lack of specific guidance related to clearance timeframes results in unclear communication between MCC and the countries regarding when approvals for disbursement requests and other related requests are granted. This poor communication could negatively affect the compact's activities.

The instructions that accompanied the June 2006 clearance matrix<sup>5</sup> indicated that MCC had 5 days to clear compact country requests, but they did not specifically identify which requests the 5 days pertained to. Thus, one country believed that MCC had 5 days to review and approve its disbursement requests. Accompanying the disbursement request is the CP report, which shows the conditions that the country has met for that particular quarter. This report is critical to MCC's decision making process, because if a compact country does not meet its CP requirements, MCC is not obligated to disburse funding for compact activities.

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<sup>5</sup> MCC's clearance matrix identifies the departments or divisions that have the authority to clear actions, issue approvals, and make no-objection decisions.

Because of unclear guidance, one country complained that MCC took 36 and 26 days to clear the country's second and third disbursement requests, respectively. Another country believed that MCC had 5 days to respond to disbursement requests and complained that MCC was not following its guidelines. This country had submitted a disbursement request to MCC in December 2006 and, as of April 2007, MCC had not cleared the request. The audit team later learned that a number of other issues had delayed the approval of this country's disbursement request. Nevertheless, based on information obtained from MCC staff, the country believed that MCC had 5 days to respond to its disbursement requests. Furthermore, because the instructions were unclear, at least one MCC program official notified his review team that it had 10 days to review and approve the disbursement request.

MCC's instructions, which accompanied a June 2006 clearance matrix, indicated that MCC had 5 days to clear country requests. The instructions did not clearly identify to which country requests the 5 days pertained. MCC officials indicated that the 5 days specified in the instructions related only to procurement requests and agreed that the information did clearly define which country requests were subject to the 5-day rule. MCC officials clarified that the disbursement agreement merely requires countries to submit their request 20 days before the end of the quarter and does not indicate a timeframe for MCC's approval.

According to the GAO's Internal Control Standards,<sup>6</sup> information should be recorded and communicated to management and others within the entity who need it in a form and within a timeframe that enables them to carry out their internal control and other responsibilities. The lack of specific guidance related to clearance timeframes has resulted in unclear communication between MCC and the countries regarding when disbursement requests and CP approvals are granted, and this could have a negative impact on a country's compact activities.

The lack of specific guidance related to clearance timeframes makes it difficult for both MCC and the compact country's operations to run effectively and efficiently. Timely communication is essential to the success of the program. Accordingly, we are making the following recommendation:

**Recommendation 2:** *We recommend that the Vice President, Department of Operations, issue guidance that clearly describes the clearance timeframe for approving country requests and related documents, such as the Conditions Precedent Report.*

## **Additional Documentation Is Needed to Justify Contracting Action**

Summary: Millennium Challenge Account–Georgia (MCA-Georgia) did not recomplete an offer after rejecting all bids, as required by the MCC's Procurement Guidelines, and awarded the contract on a single-source basis. Recompetition is required by the guidelines when bids are determined to be nonresponsive. Further, single-source selection is limited to five specific circumstances, and MCA-Georgia did not invoke any of the circumstances or request a waiver to justify the use of this procurement

<sup>6</sup> Standards for Internal Control in the Federal Government (GAO/AIMD-00-21.3.1), page 18.

method. MCC procurement officials explained that recompetition was not a viable option because of limited market interest. MCA-Georgia and MCC operations officials stated that the urgency of the work warranted the single-source award. MCC's Procurement Guidelines discourage the use of single-source selection, however, because it does not provide the benefits of competition in regard to quality and cost, lacks transparency in selection, and could encourage unacceptable practices.

During the review and testing of a CP that required MCA-Georgia to select and finalize agreement(s) for construction works, the audit identified that MCA-Georgia did not recompute an offer after rejecting all bids, as required by MCC's Procurement Guidelines. MCA-Georgia hired a consulting/engineering firm for nearly \$8.4 million on a single-source basis after the firm participated in a competition in which MCC rejected all of the bidders, including the bid from the hired firm. Specifically, MCA-Georgia held a competitive bidding process for the rehabilitation of four sections of a gas pipeline and received two bids for the work. An evaluation panel recommended that both bids be rejected. One firm was rejected because it was unqualified to perform the work; the other firm was rejected because it did not provide a required document (a work plan). MCC issued a no-objection ruling<sup>7</sup> on MCA-Georgia's conclusion.

MCC's procurement guidelines identify recompetition as a remedy when all bids are rejected for nonresponsiveness to the bid requirements. MCC procurement officials explained that recompetition was not a viable option because of limited market interest. They also explained that inviting a new bid from the other rejected firm was not reasonable because it was not qualified to do the work.

MCA-Georgia then hired the firm on a single-source basis, although the firm initially had been rejected because it did not provide a required work plan. MCA-Georgia concluded that the firm had the capability to perform the work despite the lack of a work plan. The hiring of the firm on a single-source basis was documented by a revision to the Procurement Plan, which changed the procurement method from a competitive to single-source selection. The change in the procurement method was approved by MCA-Georgia's Supervisory Board and received a no-objection ruling from MCC. MCC officials and MCA-Georgia explained that it was necessary to hire the firm on an expedited basis because of the priority of the rehabilitation work. In further discussions with MCC, MCC stated that it was not a single-source selection because a competition originally had been held. It characterized the contract as a negotiated contract, which MCC stated is permitted per Section 2.63, Rejection of All Bids, of the Procurement Guidelines. Section 2.63, cited by MCC to support its actions, addresses rejection of the bids based on cost; it does not discuss rejection based on bids being nonresponsive and, as such, is not applicable.<sup>8</sup>

<sup>7</sup> A no-objection ruling is a form of approval that means that MCC does not object to the proposed action.

<sup>8</sup> Section 2.63 of the Procurement Guidelines states, "All bids shall not be rejected and new bids invited on the same bidding and contract documents solely for the purpose of obtaining lower prices. If the lowest evaluated responsive bid exceeds the Borrower's [MCA-Georgia's] pre-bid cost estimates by a substantial margin, the Borrower [MCA-Georgia] shall investigate causes for the excessive cost and consider requesting new bids as described in the previous paragraphs. Alternatively, the Borrower [MCA-Georgia] may negotiate with the lowest evaluated bidder to try to obtain a satisfactory contract through a reduction in the scope and/or a reallocation of risk and responsibility which can be reflected in a reduction of the contract price. However, substantial reduction in the scope or modification to the contract documents may require rebidding."

MCC's procurement guidelines under Sections 2.61 through 2.64, Rejection of All Bids, provide guidance as to the actions that can be taken after rejection of all bids and are arranged based on the reason for the rejection. The reasons include effective competition is lacking, bids are not substantially responsive, or the prices are substantially higher than the budgeted amount. According to the evaluation report, MCA-Georgia rejected the bids because they were not responsive to the bidding documents (i.e., unqualified or did not provide a required document). Section 2.61 provides that "If all bids are rejected, the Borrower [MCA-Georgia] shall review the causes justifying the rejection . . . before inviting new bids." Further, Section 2.62 provides that "If the rejection is due to most or all of the bids being non-responsive, new bids may be invited from the initially pre-qualified firms, or with the agreement of the Bank [MCC] from only those that submitted bids in the first instance." MCC did not solicit new bids from the market, as noted, or request new bids from the two bidders.

The Procurement Guidelines under Section 3.6 (Direct Contracting or Single-Source Selection) provide guidance as to the five circumstances under which single-source contracting can take place:

- An existing contract for goods or works, awarded in accordance with procedures acceptable to the Bank, may be extended for additional goods or works of a similar nature.
- Standardization of equipment or spare parts, to be compatible with existing equipment, may justify additional purchases from the original supplier.
- The required equipment is proprietary and obtainable only from one source.
- The contractor responsible for a process design requires the purchase of critical items from a particular supplier as a condition of a performance guarantee.
- Exceptional cases, such as in response to natural disasters.

MCA-Georgia did not develop a written justification citing (1) the reasons that a recompetition was not feasible after rejecting all bids and (2) the necessity for a single-source selection. As a result, its procurement action may be called into question. The Procurement Guidelines encourage the use of competitive bidding and discourage the use of single-source selection. Single-source selection does not provide the benefits of competition in regard to quality and cost, lacks transparency in selection, and could encourage unacceptable practices.

There are situations in which recompetition is not viable because of limited market interest, and the urgency of the work could warrant a single-source award. Common practice among agencies that work with developing nations (such as the United Nations Development Programme and USAID) is to have a policy in place that provides for a waiver in these situations. Therefore, we are making the following recommendation:

***Recommendation 3:*** We recommend that the Vice President, Department of Accountability, develop and issue a policy requiring written justifications for deviations from the guidelines when rejecting all bids and when using single-source selection.

# EVALUATION OF MANAGEMENT COMMENTS

The MCC provided written comments to our draft report that are included in their entirety in Appendix II. In its response, the MCC agreed with the recommendations in the draft report.

For Recommendation No. 1, the MCC's Implementation Working Group has been working to develop or expand upon written guidance on a range of implementation issues, so that MCC has a transparent and consistent approach to such issues. As part of this effort, MCC plans to develop additional guidance on conditions precedent, as recommended in the audit report. One new document developed by the Working Group is the Disbursement Response Letter. The letter, in addition to other information, discusses MCC's decision to defer or waive any conditions precedent, and requests countersignature by the partner country so that there can be no confusion as to the MCC decision. In addition, in July 2007 the Deputy Chief Executive Officer called for the establishment of a team to review and revise MCC's reporting requirements and guidance for MCA Accountable Entities. This group has been established and will review all required quarterly reports, including the CP report. It will issue recommendations to MCC's Deputy CEO about any changes to reporting formats, frequency and guidance in mid October 2007.

For Recommendation No. 2, the MCC agrees that the specific timeframe for response to a country disbursement request is not as clear as it could be, and will issue guidance clarifying this timeframe as recommended by December 31, 2007.

For Recommendation No. 3, the MCC concurred with the recommendation and indicated that Part 7 of MCC's Program Procurement Guidelines state that: "On a case by case basis, MCC may grant waivers of certain provisions of the MCC Program Procurement Guidelines as applicable to a particular procurement. Such waiver shall be in writing and shall be effective only to the extent specifically set forth in such writing." In response to requests for further clarification on this issue, we are in the process of finalizing a Guidance note specific to such waivers which will be completed by December 31, 2007.

While we appreciate MCC's issuing guidance on the granting of such waivers as we recommended, we would like to point out that MCC's Program Procurement Guidelines referred to were issued on May 22, 2007. Our fieldwork was conducted during the week of March 12, 2007 and used the World Bank modified procurement guidelines in effect at the time, which were dated April 7, 2006 and did not include a waiver provision.

Based upon MCC's written comments, the OIG considers that a management decision has been reached on the recommendations.

# SCOPE AND METHODOLOGY

## Scope

The Millennium Challenge Corporation's (MCC's) Office of Inspector General audited MCC's conditions precedent (CPs) program in accordance with generally accepted government auditing standards to determine whether MCC ensured that CPs were successfully met and properly implemented before the compact entered into force and before initial and subsequent disbursements.

The audit included tests and reviews of selected internal controls integral to the CP process, including (1) appropriate reviews and approvals of relevant CP documentation; (2) adequate verification of disbursements for compact administration and activities; (3) documentation of key elements of the entry-into-force and initial/subsequent disbursements requirements; and (4) controls over the compact procurement process.

The scope included MCC's disbursements of \$62.1 million to six countries<sup>9</sup> for the period from January 2004 to March 2007.

Audit fieldwork was conducted at MCC's headquarters in Washington, DC, between January 24, 2007, and April 13, 2007. Fieldwork conducted between March 4, 2007, and March, 17, 2007, included site visits to Praia, Cape Verde; Tbilisi, Republic of Georgia; Managua, Leon, and Chinandega, Republic of Nicaragua; and Tegucigalpa, Republic of Honduras.

## Methodology

In planning and conducting this audit, the audit team interviewed MCC management and staff from MCC's office of the general counsel, country directors, departments of accountability and operations, procurement specialists, and program officers.

To assess internal controls associated with the CPs in compact-eligible countries, the audit team interviewed Millennium Challenge Account (MCA) management and staff and examined relevant documentation such as the country's compacts, procurement agreements and plans, governance agreements, monitoring and evaluation plans, disbursement requests and agreements, CP status reports, and compact activity status reports.

In addition, the audit team performed the following tasks:

- Reviewed compact agreements and applicable documents relevant to the CP process to obtain an understanding of the process.
- Identified and judgmentally selected six eligible compact countries that have entered into force and received initial or subsequent disbursements and used these countries as a basis for conducting this audit.

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<sup>9</sup> Armenia: \$3.6 million; Cape Verde: \$7.5 million; Georgia: \$25.5 million; Honduras: \$7.1 million; Madagascar: \$14.5 million; Nicaragua: \$3.9 million.

- Reviewed and selected procurement contracts and related documentation and files, including procurement plans, evaluation reports, and payments to service providers.
- Interviewed MCC and MCA contractors and service providers.

# MANAGEMENT COMMENTS



MEMORANDUM

July 24, 2007

TO: John Phee  
Assistant Inspector General for the Millennium Challenge Corporation

FROM: Michael Ryan /s/  
Vice President for Administration and Finance

SUBJECT: MCC Management Comments on Audit of the Millennium Challenge Corporation's  
Management of its Conditions Precedent in its Compact Agreements

The MCC appreciates the opportunity to respond to the text and recommendations of this audit. While the MCC would like to clarify two of the findings contained in the audit results, the MCC concurs with all recommendations contained in the audit, and has already addressed one of these recommendations.

***Recommendation 1:** We recommend that the Deputy Chief Executive Officer, by means of the current Implementation Working Group or a newly established working group, develop and issue, specific guidelines that describe how conditions precedent will be established, defined, revised, and reported.*

MCC concurs with this recommendation. The Implementation Working Group, which is chaired by the Deputy Vice President of Operations, has been working to develop or expand upon written guidance on a range of implementation issues, so that MCC has a transparent and consistent approach to such issues. In the past few months, the MCC has issued clear and consistent Program Procurement Guidelines, Financial Reporting Instructions, and other guidance to be followed by MCC partner countries. As part of this effort, MCC plans to develop additional guidance on conditions precedent, as recommended in your audit report.

One new document developed by the Working Group is the Disbursement Response Letter. This is a standard letter that will be sent to all partner countries, beginning with the fourth quarter FY 2007 set of disbursement requests, in order to clearly notify the country of MCC's decision regarding its disbursement request and specify any adjustments to that request. It also discusses MCC's decision to defer or waive any conditions precedent, and requests countersignature by the partner country so that there can be no confusion as to the MCC decision. A copy of the framework for this letter is attached.



In addition, in July 2007 the Deputy Chief Executive Officer called for the establishment of a team to review and revise MCC's reporting requirements and guidance for MCA Accountable Entities. This group has been established and will review all required quarterly reports, including the CP report. It will issue recommendations to MCC's Deputy CEO about any changes to reporting formats, frequency and guidance in mid October 2007. MCC hopes to apply these new formats and guidance to the Fiscal Year 2008 second quarter reporting cycle.

***Recommendation 2:*** *We recommend that the Vice President, Department of Operations, issue guidance that clearly describes the clearance timeframe for approving country requests and related documents, such as the Conditions Precedent Report.*

MCC concurs with this recommendation. However, we would like to clarify the findings associated with it. As the report correctly states, the new MCC internal clearance matrix gives individual clearers five business days to clear a specific report, such as the conditions precedent report, that is submitted with a country's disbursement request. However, the matrix does not require that the entire disbursement request be cleared and a response provided to the country within five days. Rather, MCC asks countries to submit their disbursement request 20 calendar days before the end of a quarter, with the goal of responding to the request by the first day of the following quarter, either with the first month disbursement tranche, or with specific concerns or adjustments as contained in the Disbursement Response Letter.

MCC agrees that the specific timeframe for response to a country on its disbursement request is not as clear as it could be, and will issue guidance clarifying this timeframe as recommended by December 31, 2007. However, better guidance is only one part of ensuring adherence to timely submissions and review of disbursement requests and related reporting documentation. MCC's experience is that the process of receiving, reviewing and approving reports and disbursement requests can take more than 20 days, due primarily to the varying capacity of countries to prepare quality reports. One goal of the reporting review team (mentioned above) is to understand the cause of delays in the preparation and review of reports, and make recommendations to improve the process. This will be an on-going effort on behalf of MCC that will not be fully resolved by having clearer timeline guidance.

***Recommendation 3:*** *We recommend that the Vice President, Department of Accountability, develop and issue a policy requiring written justifications for deviations from the guidelines when rejecting all bids and when using single-source selection.*

MCC concurs with the recommendation. Part 7 of MCC's Program Procurement Guidelines state that: "On a case by case basis, MCC may grant waivers of certain provisions of the MCC Program Procurement Guidelines as applicable to a particular procurement. Such waiver shall be in writing and shall be effective only to the extent specifically set forth in such writing." In response to requests for further clarification on this issue, we are in the process of finalizing a Guidance note specific to such waivers which will be completed by December 31, 2007.

MCC does believe that the finding includes a misunderstanding of MCC's program procurement process in the case described in the audit. In this particular case, a competitive process was run,

resulting in only two bids, both of which were non-responsive. Market research demonstrated that a new procurement was not likely to result in more bidders and one of the bidders was not technically competent to perform the work. Section 2.62 of the Procurement Guidelines allows that when the rejection of all bids is “...due to most or all of the bids being non-responsive, new bids may be invited ... with approval of MCC from only those that submitted bids in the first place.” In accordance with section 2.62, a new bid was then requested from one of the two original bidders. In sum, this was not a sole-source bid; rather, the bidder was selected based on an open competitive tender, but the contract was negotiated. We recognize that in amending the Procurement Plan to reflect this we documented the case incorrectly and that has caused some confusion. We also recognize that the cancellation itself was not transparent and as a result we have added the following to section 2.64 of the Procurement Guidelines: “Within two weeks of the rejection of all bids, the MCA Entity shall post at *dgMarket* and the MCA Entity’s website ... notification of the cancellation of procurement. The notification shall identify the procurement and state briefly the reason for canceling the procurement. The same information shall be sent to all bidders who have submitted bids.” To further assist in clarification of such cases going forward, we intend to develop a guidance paper on rejection of bids.

**U.S. Agency for International Development**  
**Office of Inspector General**  
1300 Pennsylvania Avenue, NW  
Washington, DC 20523  
Tel: (202) 712-1150  
Fax: (202) 216-3047  
**[www.usaid.gov/oig](http://www.usaid.gov/oig)**